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In the Supreme Court of the United States

OCTOBER TERM, 1955

No. 883

In the Matter of the Tax Liability of NORDA ESSENTIAL OIL AND CHEMICAL COMPANY, INC., of the Lower Manhattan District, PETITIONER

v.

UNITED STATES OF AMERICA

ON PETITION FOR A WRIT OF CERTIORARI TO THE UNITED STATES COURT OF APPEALS FOR THE SECOND CIRCUIT

BRIEF FOR THE RESPONDENT IN OPPOSITION

OPINIONS BELOW

The United States District Court for the Southern District of New York filed no opinion. The opinion of the Court of Appeals (Pet. 1a-4a) is not yet reported.

JURISDICTION

The judgment of the Court of Appeals was entered on March 7, 1956. The petition for a writ of certiorari was filed on April 19, 1956. The juris-

diction of this Court is invoked under 28 U.S.C., Section 1254.

QUESTION PRESENTED

Whether the Court of Appeals, affirming the District Court, correctly held that the taxpayer was required—in connection with an investigation of its tax liability for 1952—to produce books and records which had been previously examined in connection with a determination of its liability for prior years, where it was not disputed that such books and records contained information germane to a determination of the taxpayer's correct liability for 1952.

STATUTE INVOLVED

Internal Revenue Code of 1954:

> SEC. 7602. EXAMINATION OF BOOKS AND WITNESSES.
>
> For the purpose of ascertaining the correctness of any return, making a return where none has been made, determining the liability of any person for any internal revenue tax or the liability at law or in equity of any transferee or fiduciary of any person in respect of any internal revenue tax, or collecting any such liability, the Secretary or his delegate is authorized—
>
> (1) To examine any books, papers, records, or other data which may be relevant or material to such inquiry;
>
> (2) To summon the person liable for tax

or required to perform the act, or any officer or employee of such person, or any person having possession, custody, or care of books of account containing entries relating to the business of the person liable for tax or required to perform the act, or any other person the Secretary or his delegate may deem proper, to appear before the Secretary or his delegate at a time and place named in the summons and to produce such books, papers, records, or other data, and to give such testimony, under oath, as may be relevant or material to such inquiry * * *.

(26 U.S.C. 1952 ed., Supp. II, Sec. 7602.)

SEC. 7604. ENFORCEMENT OF SUMMONS.

(a) *Jurisdiction of District Court.*—If any person is summoned under the internal revenue laws to appear, to testify, or to produce books, papers, records, or other data, the United States district court for the district in which such person resides or is found shall have jurisdiction by appropriate process to compel such attendance, testimony, or production of books, papers, records, or other data.

(b) *Enforcement.*—Whenever any person summoned under section 7602 neglects or refuses to obey such summons, or to produce books, papers, records, or other data, or to give testimony, as required, the Secretary or his delegate may apply to the judge of the district

court or to a United States commissioner for the district within which the person so summoned resides or is found for an attachment against him as for a contempt. It shall be the duty of the judge or commissioner to hear the application, and, if satisfactory proof is made, to issue an attachment, directed to some proper officer, for the arrest of such person, and upon his being brought before him to proceed to a hearing of the case; and upon such hearing the judge or the United States commissioner shall have power to make such order as he shall deem proper, not inconsistent with the law for the punishment of contempts, to enforce obedience to the requirements of the summons and to punish such person for his default or disobedience.

* * * * *

(26 U.S.C. 1952 ed., Supp. II, Sec. 7604.)

* * * * *

SEC. 7605. TIME AND PLACE OF EXAMINATION.

* * * * *

(b) *Restrictions on Examination of Taxpayer.*—No taxpayer shall be subjected to unnecessary examination or investigations, and only one inspection of a taxpayer's books of account shall be made for each taxable year unless the taxpayer requests otherwise or unless the Secretary or his delegate, after investigation, notifies the taxpayer in writing that an additional inspection is necessary.

(26 U.S.C. 1952 ed., Supp. II, Sec. 7605.)

STATEMENT

In 1955, a special agent of the Intelligence Division, Internal Revenue Service, United States Treasury Department, was conducting an investigation of the tax liability for 1952 of the taxpayer, Norda Essential Oil and Chemical Company, Inc. In connection with that investigation, which had commenced about January, 1954, the special agent, acting under authority of Section 7602 of the Internal Revenue Code of 1954, *supra*, pp. 2-3, on April 19, 1955, issued a summons requiring the taxpayer to produce the following books and papers for examination (R. 4a, 21a, 7a-8a):

> 1. Voucher Registers and Cash Receipts & Disbursements books for the years 1950 and 1951.
>
> 2. Paid invoices and cancelled checks representing acquisitions to "Trucks", "Equipment", and "Construction Machinery" accounts during the years 1950 and 1951 as set forth in Schedule I of the 1952 Corporation income tax return.
>
> 3. All paid vouchers representing plant, machinery or equipment leased to or otherwise provided for or to Fruit Industries of Bradenton, Fla.

By letter of April 28, 1955, the taxpayer's counsel informed the special agent that he had advised the taxpayer that it was not required to furnish any books and documents covering the years 1950 and 1951, since (1) "the statute of limitations has run for 1950 and 1951", and (2) "the said years were

the subject of a prior investigation by the Internal Revenue Service."[1] (R. 16a.)

On May 2, 1955, pursuant to the summons, representatives of the taxpayer appeared at the special agent's office. They were informed by an Internal Revenue agent, who was assisting the special agent in connection with the investigation, that the Internal Revenue Service desired the 1950 and 1951 records "in order to verify the depreciation schedule attached to the income tax return of Norda for the year 1952" and "to determine if the Norda Essential Oil & Chemical Co., Inc. had expensed items which should have been capitalized." The taxpayer's representative, explaining that "the only effect [of examining the records for 1950 and 1951] could be to give Norda Essential Oil and Chemical Co., Inc., a larger deduction by way of depreciation, and thus less taxable income for the year 1952," there-

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[1] The full text of the letter follows (R. 16a-17a):

Norda Essential Oil and Chemical Company has forwarded to me the Form 860-A, Summons to Appear, to Testify, and to Produce Books, Etc., addressed to John Horak and Norda Essential Oil and Chemical Company, dated April 19, 1955.

I have advised the Norda Essential Oil and Chemical Company, Inc. to produce the documents covered by the summons for the year 1952. However, I have advised the Norda Essential Oil and Chemical Company that the statute of limitations has run for 1950 and 1951; that the said years were the subject of a prior investigation by the Internal Revenue Service and that they are not required to furnish the documents and books you have requested for the years 1950 and 1951.

A representative of this office will appear at your office at 10:00 a.m. on Monday, May 2, in accordance with the summons.

upon offered on behalf of the taxpayer "to accept the depreciation schedule as set forth in the income tax return for the year 1952", in order to eliminate "the necessity of any inquiry into those years [1950 and 1951] for the purposes requested by Internal Revenue." The offer was declined. The taxpayer refused, however, to produce the 1950 and 1951 records. (R. 6a, 20a, 21a.)

Thereafter, on May 11, 1955, upon the affidavit of the special agent setting forth the facts as to the issuance of the summons and the refusal to comply therewith, the United States District Court for the Southern District of New York entered an *ex parte* order requiring the taxpayer to appear on May 16, 1955, and produce the books and records designated in the summons. The special agent's affidavit alleged that he was investigating the taxpayer's "tax liability for the year 1952", and that "the books and records demanded in the summons are required to authenticate the deduction for depreciation taken in Schedule I of the 1952 Corporation income tax return." (R. 2a-6a.)

On May 16, 1955, upon the taxpayer's motion, supported by the affidavits of its representatives, the District Court (1) ordered the special agent to show cause, on May 24, 1955, why its *ex parte* order should not be vacated, and (2) stayed all proceedings to enforce the provisions of that order. (R. 8a-9a.)

The affidavits in support of the taxpayer's motion admitted the following facts: that the taxpayer "is a party to a tax inquiry * * * to

determine liability for taxes for the year 1952"; that the taxpayer had been informed that "the Internal Revenue Service desired these records in order to verify the depreciation schedule attached to the income tax return of Norda for the year 1952"; and that the taxpayer, through its representative, thereupon offered—on its hypothesis that an examination of the requested records for 1950 and 1951 would permit a larger depreciation deduction for 1952—to accept the depreciation schedule as set forth in its 1952 return, "thus waiving any additional depreciation which Norda Essential Oil & Chemical Co., Inc. might be entitled to receive for the year 1952." (R. 10a, 20a.)

The affidavit filed by the special agent in reply declared that the summons issued "clearly stated * * * that the information requested * * * directly relates to and bears on the figures set forth in Schedule I of the 1952 corporation income tax return * * *." (R. 24a.) The contents of Schedule I were annexed to and were made part of the special agent's affidavit. (R. 27a-31a.)

On May 25, 1955, the District Court denied the motion to vacate its *ex parte* order dated May 11, 1955. The Court of Appeals affirmed. (R. 31a; Pet. 1a-4a.)

ARGUMENT

1. In holding that the taxpayer was required, in connection with the investigation as to its liability for 1952, to produce 1950 and 1951 records germane to a determination of its depreciation

allowance for 1952, the decisions below correctly enforce the investigatory authority conferred by Section 7602 of the Internal Revenue Code of 1954, *supra*, pp. 2-3. That section provides that, for the purpose of ascertaining the correctness of any return or determining the tax liability of any person, the Secretary or his delegate is authorized to examine any books, papers, records, or other data which may be relevant or material to such inquiry, and to cause them to be produced for that purpose.

The requested records for 1950 and 1951 were obviously required in order to verify the correctness of the taxpayer's 1952 return. As the Court of Appeals noted (Pet. 2a): "Specifically involved are depreciation deductions claimed by appellant in its 1952 return totaling $107,145.12 upon assets, of which those purchased in 1950 and 1951 alone amounted to $462,268.65." And, as the court below further noted, the requested records were relevant not only to determine (Pet. 3a) "the number and amount" of purchases made in the prior years, but also whether they were in fact made by the taxpayer "or by a business associate, Fruit Industries of Bradenton, Fla. * * *." In the circumstances, the Court of Appeals correctly concluded that further "exploration", through compulsory production of the 1950 and 1951 records, was entirely warranted. Cf. *Falsone* v. *United States*, 205 F. 2d 734, 742-743 (C.A. 5th), certiorari denied, 346 U.S. 864; *Moraine Hotel Co.* v. *Commissioner*, 41 F. 2d 725, 726 (C.A. 7th); *Zimmer-*

mean v. *Wilson*, 105 F. 2d 583 (C.A. 3d); *United States* v. *United Distillers Products Corp.*, 156 F. 2d 872 (C.A. 2d).

Significantly, the taxpayer does not contend that the requested records are in fact irrelevant or immaterial to a determination of its correct liability for 1952. On the contrary, its admission (Pet. 11) that "The depreciation schedule [R. 27a-31a] which the Special Agent seeks to 'authenticate' contains assets purchased as far back as 1939 *and in all intervening years through 1952*" (emphasis added), together with its offer (R. 20a) to waive the alleged benefit for 1952 of any adjustment to depreciation which might result from a check of the 1950 and 1951 records, demonstrates the propriety of the summons to produce those records.

The taxpayer, invoking Section 7605(b) of the 1954 Code, *supra*, p. 4, emphasizes the fact that its books and records have already been examined in connection with the taxable years 1950 and 1951. But Section 7605(b) merely provides that, normally, only one inspection of a taxpayer's books shall be made "for each taxable year." The undisputed fact here is that the summons in question was issued in connection with a first investigation as to 1952; the 1950 and 1951 books and records had never been previously inspected in connection with the investigation as to the taxable year 1952. The basic fallacy of the taxpayer's reliance upon Section 7605(b) is that it ignores the plain meaning of the phrase, "for each taxable year," and

unwarrantedly assumes—in the face of the patent relevance of the 1950 and 1951 records to a determination of the correctness of the 1952 return—that inspection of those records was unnecessary simply because they had already been inspected in connection with an investigation as to prior years. Cf. *Falsone* v. *United States, supra; Moraine Hotel Co.* v. *Commissioner, supra.* The same fallacy underlies the irrelevant contention that the statute of limitations had run for the taxable years 1950 and 1951 unless fraud could be shown. The statute had not run for 1952, the taxable year in question, and since the books and records for 1950 and 1951 show transactions which have a direct bearing on the correct tax liability for 1952, it was not necessary to allege fraud in order to compel their production.

2. Contrary to the taxpayer's claim (Pet. 7), there is no conflict between the decision below and *Local 174* v. *United States* (C.A. 9th), decided December 7, 1955 (1956 P-H, par. 72,362). In the instant case, in which the taxpayer itself was summoned to produce its own specifically described records covering only a period of two years, and for the purpose of checking its tax liability for only the one year 1952 (R. 7a-8a), the material before the District Court on the taxpayer's motion to vacate that court's *ex parte* order made apparent the relevancy of the requested records to a determination of the correctness of the taxpayer's 1952 return. (R. 18a-31a.) Consequently, the District Court was not required to conduct any further

proceedings for the purpose of satisfying itself as to the relevancy and materiality of the 1950 and 1951 records.[2]

In the *Local 174* case, on the other hand, a summons was issued directing a third party, a union, to produce in connection with an investigation of the tax liability of one of its officials for the calendar years 1943 to 1953, inclusive, all records and books of account, unspecified, which for that eleven-year period "in any way" referred or related to transactions between the union and the taxpayer, his wife, "or any other person acting for * * * either of them." (Pet. 5a.) The District Court, upon the union's failure to comply, ordered it to produce, "for so long * * * as may be necessary to afford full and complete inspection," all of the following material covering the entire period: cash books, day books, bank deposit slips, cancelled checks, check stubs, loan ledger cards, individual payroll records, retained copies of financial statements and of tax returns or reports, and all bookkeeper's work sheets used in the preparation of the financial statements and tax returns. (Pet. 6a-7a.) In those far different circumstances, the Ninth Circuit concluded (Pet. 11a-12a) that the District Court had failed to exercise its judgment as to how far the voluminous materials sought

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[2] The taxpayer asserts (Pet. 12) "that the Special Agent's real purpose for seeking access to the books is to fish for evidence of fraud." But the affidavits before the District Court contained nothing which supported or even suggested this belated allegation.

from the union were relevant to the official's tax liability. As the court below observed, correctly distinguishing the *Local 174* decision (Pet. 3a-4a), there was no comparable issue of relevancy here, and the claim of conflict fails.

CONCLUSION

It is respectfully submitted that the petition for a writ of certiorari should be denied.

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